

INFRASTRUCTURE REPORT

CITY OF MORGAN HILL



NOVEMBER 2014

Purpose of Report

The City of Morgan Hill's infrastructure is a very diverse system that supports a number of essential community needs and is utilized by both residents and visitor. Maintenance of this infrastructure is an expensive endeavor for the City, and one that is vital for public safety, economic development, and quality of life, all of which are critical elements for the City as it strives to ensure Morgan Hill remains a sustainable, vibrant, and quality community. This report is intended to provide a detailed look at the overall funding needs for each of the City's infrastructure categories and initiate the community discussion on the range of solutions available to address any gaps by identifying and quantifying the maintenance needs of the City's infrastructure.

Overview

The City of Morgan Hill has the responsibility of planning, constructing, and maintaining infrastructure to meet the needs of the community, which can be divided into two categories: 1) those needed to accommodate new growth; and 2) those needed to maintain the existing system. The City utilizes "development impact fees" charged to new development in order to mitigate the impacts of new growth on the existing community. This funding source can only be used to pay for projects to expand the City's infrastructure capacity and not for ongoing maintenance. To fund maintenance activities, the City primarily relies on General Fund taxes or customer charges. This report attempts to answer two foundational questions:

1. What are the City's existing infrastructure maintenance needs?
2. Are there existing funding gaps?

Existing Infrastructure Highlights

122 Miles of Streets

3,700 Street Lights

45 Traffic Signals

60 Acres of Maintained Parks

13 Public Facilities

18 Sports Fields

4 Swimming Pools

The City owns, operates and maintains a variety of infrastructure assets. These can be broken down into five categories:

- Streets
- Water and Sewer Systems*
- Parks and Trails
- Landscape Assessment District Facilities
- City Buildings and Facilities

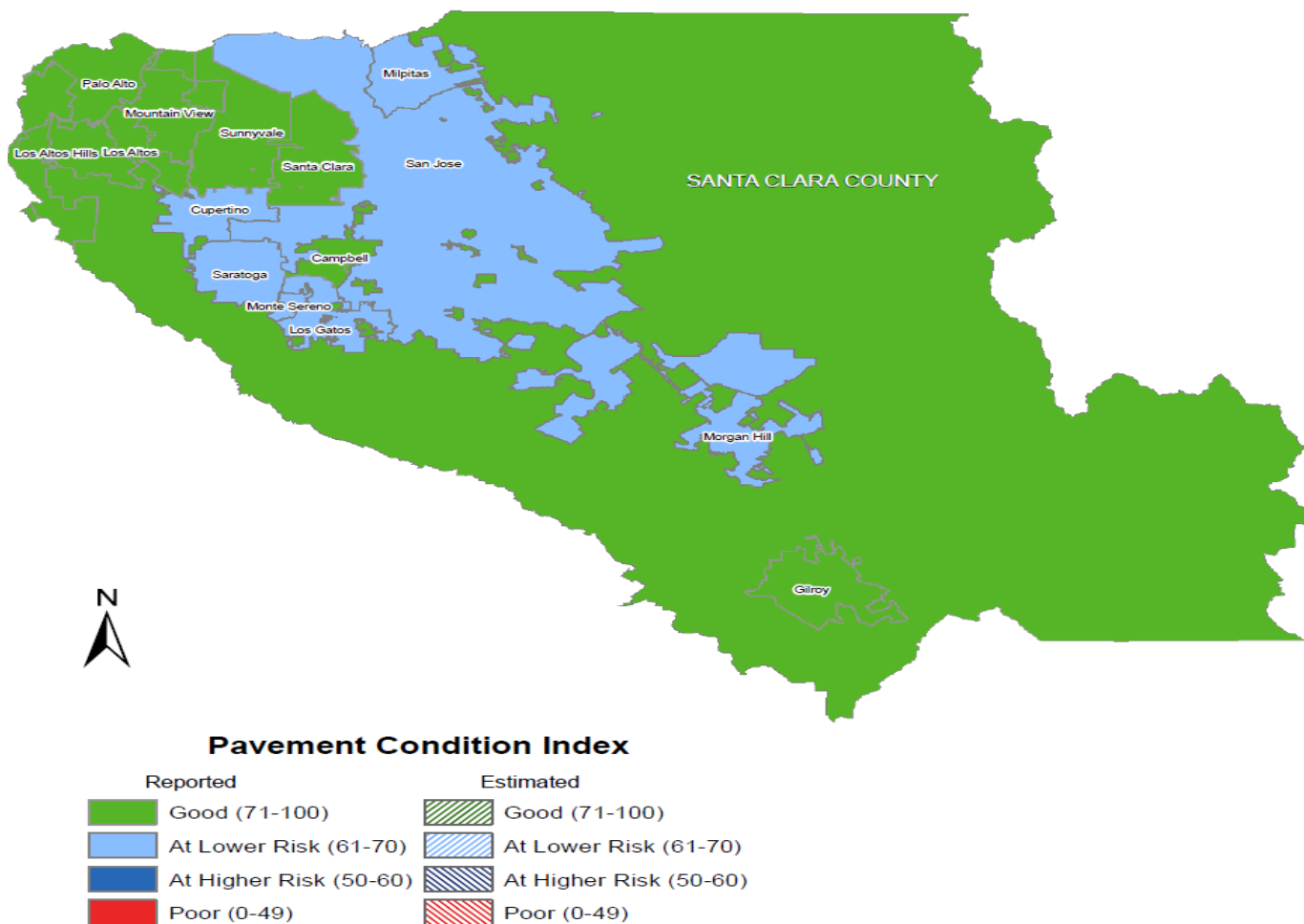
** The City's water and sewer utilities are a vital element of the City's infrastructure, these utilities are not addressed in this report because they are paid for by customer charges and do not rely on the General Fund.*

Each of the categories also has two subcategories of maintenance. The first subcategory is baseline ongoing maintenance services (e.g., tree trimming, filling of potholes, janitorial, and grass mowing). The second is capital projects relating to the replacement or major repair of existing infrastructure resources (e.g., pavement rehabilitation, full replacement of a park playground, and replacement of a heating unit).

During the previous decade, the City made significant investments in infrastructure to meet the needs of a growing city. During that timeframe, the City utilized the Redevelopment

Agency to finance construction of new infrastructure and to maintain those assets. With the demise of redevelopment in 2011, the City lost a major funding source for the rehabilitation, renovation, reconstruction, and modernization of infrastructure.

Further impacting the City's ability to fund infrastructure maintenance in the last decade, has been the decline in the single largest funding source for street infrastructure maintenance, the "gas tax." Due to the growth in more fuel-efficient and alternative fuel vehicles, gas tax revenues have fallen in a relative sense and are projected to continue declining which has created a statewide problem. The recently released Local Streets and Roads Assessment for California (Appendix B) indicates that there is a backlog of \$40 billion in deferred street maintenance and an annual funding shortfall of \$7.8 billion state wide for street maintenance. The report identifies that 80% of the states roads belong to Cities and Counties, and that most are struggling to cope with increasing deferred maintenance backlogs and funding gaps. The following map provides an updated look at the condition of streets and roads across the county.



Funding

In 2013, the City Council established "Financing and Advocating for Infrastructure Improvements" as one of 2013 priorities. In May of that year, the Council received the results of the Safe and Sustainable Streets Infrastructure Study, which identified street

maintenance funding as inadequate for future years. In 2014, the Council again prioritized infrastructure and requested that City staff develop this comprehensive report that identifies, quantifies, and prioritizes the needs to maintain the City's entire existing infrastructure.

Currently, the City's General Fund is relied upon to supplement other dedicated funds in supporting infrastructure maintenance. The Fiscal Year 14/15 General Fund expenses were \$32.6 million, of which \$21.5 million were discretionary. The following diagram illustrates how the City utilizes its discretionary General Fund expenses.



Recent Infrastructure Investments

LED retrofit of street lights

Increased funding for sidewalk replacement

Reinstated grid pruning on 4 year cycle

Solar installations at 3 city facilities

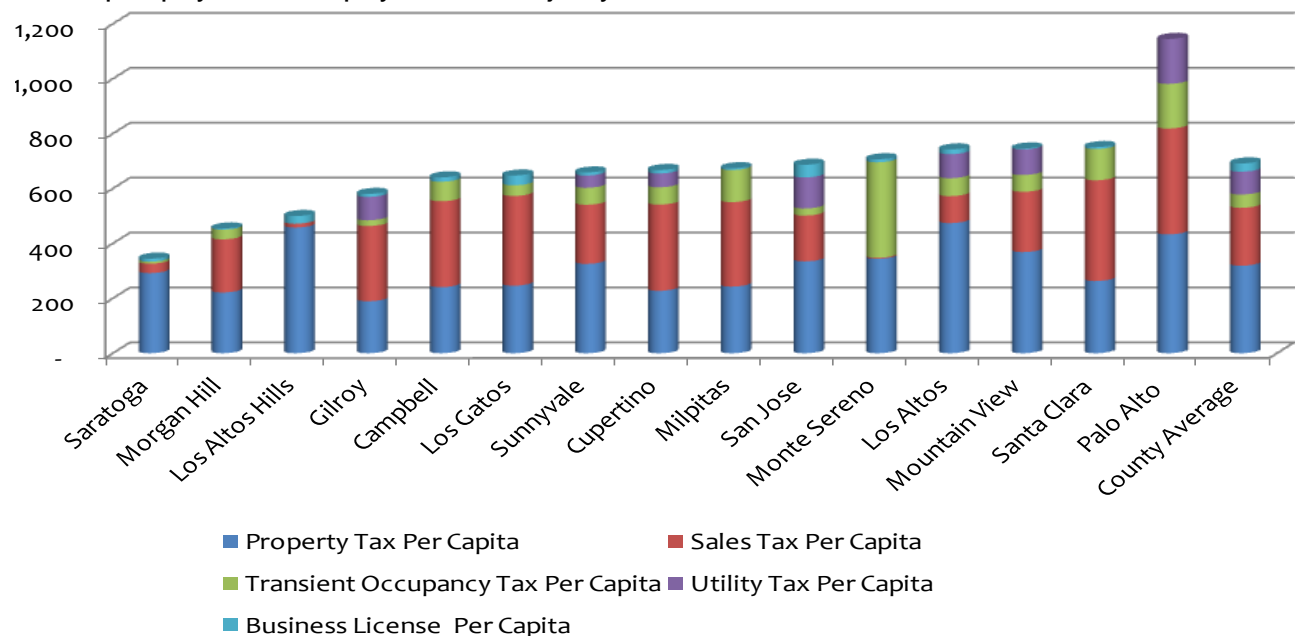
Replacement of street name signs

Replacement of turf with low water irrigation or other surfaces

Funded annual City parking lot maintenance on 8 year cycle

As indicated, the City currently spends 4.1 percent of discretionary General Fund dollars on maintenance of its streets through pavement rehabilitation, capital improvements and ongoing base level street maintenance services. It is important to understand: 1) the City's

discretionary General Fund revenue is primarily obtained through taxes (Property Tax, Sales Tax and Transient Occupancy Tax) and is much more limited than that of many other communities as Morgan Hill's per capita tax revenue ranks among the lowest in the County, 2) facility maintenance of recreation centers is primarily paid for by user charges, this amount of discretionary dollars is required, and 3) the City's parks rely on voluntary developer payments to pay for the majority maintenance activities.

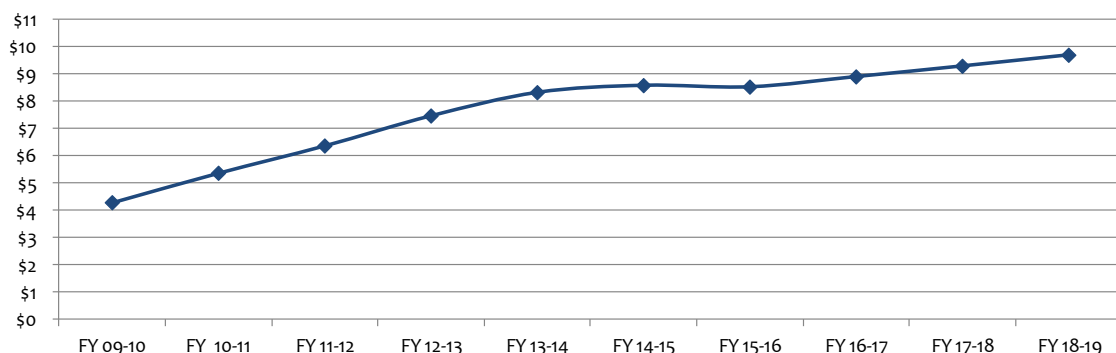


Ongoing maintenance of these assets is performed using a variety of means funded through a variety of sources. The matrix in Table 1 outlines the primary funding for each of the subcategories:

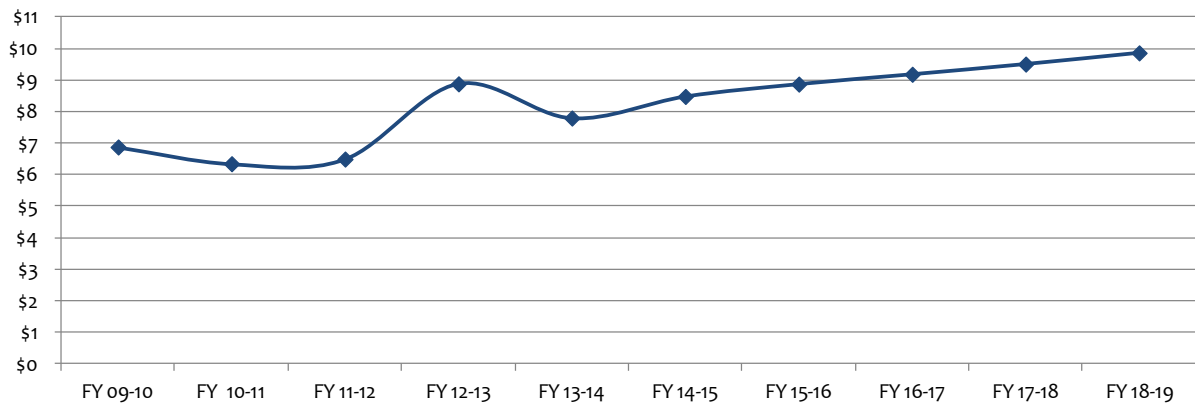
Table 1. Category of Maintenance	Primary Funding Sources
Street Maintenance Capital Repair and Replacement	Gas Tax Measure B – Vehicle Registration Fees General Fund Discretionary Revenue Grant Funds – Includes On Bay Area Grant
Street Maintenance Base Services	Gas Tax General Fund Discretionary Revenue Sewer Fund – Customer Charges Water Fund – Customer Charges
Park Maintenance Capital Repair and Replacement	Park Maintenance Fund – Developer Voluntary Contributions General Fund Discretionary Revenue Grant Funds
Park Maintenance Base Services	Park Maintenance Fund – Developer Voluntary Contributions General Fund Discretionary Revenue
Landscape Assessment District Capital Repair and Replacement	Property Tax Assessments for those within District
Landscape Assessment District Capital Repair and Replacement	Property Tax Assessments for those within District
Building Maintenance Capital Repair and Replacement	General Fund Non-discretionary Revenue (Recreation Charges) General Fund Discretionary Revenue Other funds based on percentage use of facilities
Building Maintenance Base Services	General Fund Non-discretionary Revenue (Recreation Charges) General Fund Discretionary Revenue Other funds based on percentage use of facilities

As is indicated in the chart, with the exception of the Landscape Assessment District, all of the other infrastructure areas outlined are supported by General Fund Discretionary Revenue. The next two graphs provide a history and forecast of the two largest tax revenue sources for General Fund Discretionary Revenue, sales tax and property tax:

Sales Tax Revenue



Property Tax Revenue



Both sources of taxes show modest increases in revenue over future years, but these increases in revenue will be necessary to account for inflationary operating costs for the City. However, as was previously mentioned, the Gas Tax revenue will not be able to keep up with inflationary costs and is forecasted to remain flat for the next five years.

Fuel Tax Revenue

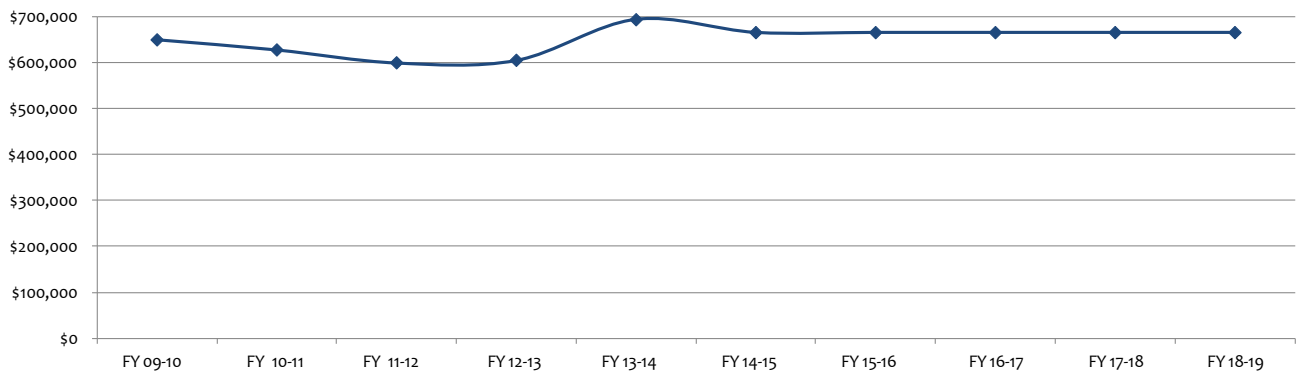


Table 2 shows the background documents that are now available to guide The City's infrastructure planning.

In the recent past, the funding shortfall for maintenance of streets has been well documented. Our most recent Pavement Management Report shows a backlog of \$20.5 million dollars in maintenance.

Recent analysis of maintenance in the areas of City Buildings and Facilities, Parks and Trails, and Landscape Assessment District Facilities shows that funding shortfalls exist in these areas as well, though not at as significant a level as streets. Ongoing maintenance in these areas has limited the backlog of deferred maintenance and, in most cases, had a greater impact on service levels. In some of these areas, maintenance levels have been reduced and reserve

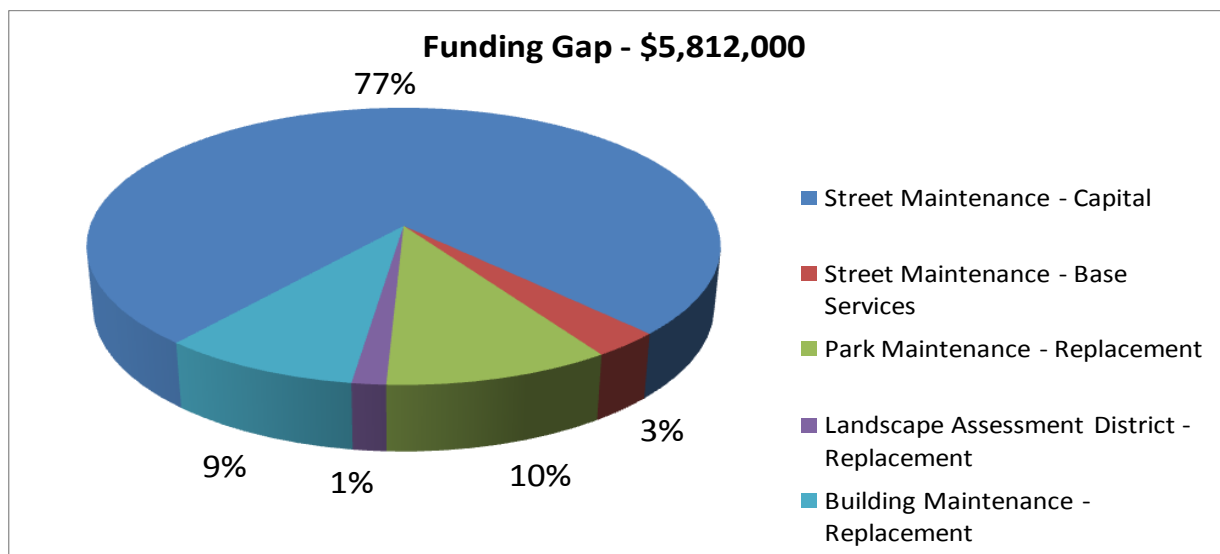
Table 2. Infrastructure Funding Planning Documents

Sustainable Streets Study – May 2013
Biennial Pavement Condition Report – Mar 2014
Biennial Pavement Management Report – April 2014
Park Asset Replacement Inventory - October 2014
Annual Engineers Report for LAD – June 2014
Building Future Replacement Plan - October 2014

funding for future maintenance has not occurred or may not be adequate for future needs. Currently, it is estimated that there is a \$5.8 million annual maintenance funding shortfall across all infrastructure categories. Table 3 provides a comparison of the City's existing funding levels and the amount required to be considered sustainable. For the purpose of this report, the term sustainable is defined as the following: "The level of annual funding required to ensure the City's infrastructure is adequately maintained for use in the present, avoids deferring maintenance costs to a later date, and funds accrues for future known replacement over the life period of each infrastructure asset."

Table 3. Category of Maintenance	Current Annual Funding Level	Sustainable Annual Funding Level	Annual Funding Shortfall
Street Maintenance Capital Repair and Replacement*	\$ 753,000	\$ 5,200,000	\$ (4,447,000)
Street Maintenance Base Services	\$ 1,888,000	\$ 2,066,000	\$ (178,000)
Park Maintenance Capital Repair and Replacement	\$ -	\$ 586,000	\$ (586,000)
Park Maintenance Base Services	\$ 1,027,000	\$ 1,027,000	\$ -
Landscape Assessment District Capital Repair and Replacement	\$ -	\$ 88,000	\$ (88,000)
Landscape Assessment District Base Services	\$ 180,000	\$ 180,000	\$ -
Building Maintenance Capital Repair and Replacement	\$ 389,000	\$ 903,000	\$ (514,000)
Building Maintenance Base Services	\$ 2,654,000	\$ 2,654,000	\$ -
TOTAL	\$ 6,891,000	\$ 12,703,000	\$ (5,812,000)

* 2014/15 includes additional one-time funding for street maintenance of \$1,544,000 above the \$753,000.

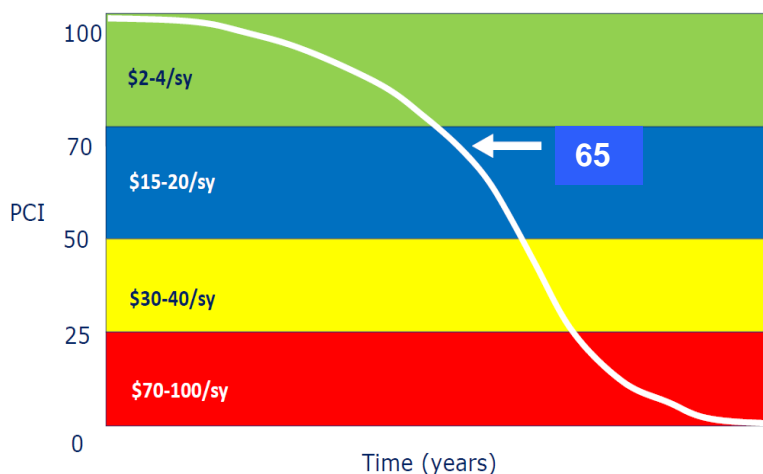
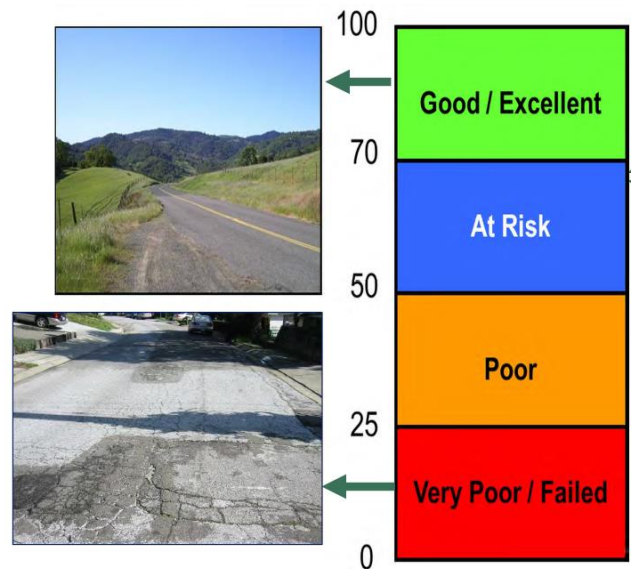


Street Maintenance remains, by far, the largest area of need in terms of funding for infrastructure at 80%, while replacement of existing Park Assets is the second largest need making up 9% of the unfunded need. Some degree of future replacement savings has been made in the Landscape Assessment District and Building Maintenance areas. The amount of funding set aside varies by facility and by assessment district subarea. The funding details, challenges, and policy questions for each of these areas are outlined in the following sections of the report.

Street Maintenance

The City Council identified the “Streets Infrastructure” as a vital community element and one that needs a great deal of attention. The City has approximately 122 miles of local streets with a variety of attached ancillary elements including: street trees, traffic signals, signs, curb & gutter, streetlights, storm drains, bridges, medians and planters, furnishings, guard rails, parking lots, and sidewalks.

The greatest concern in the area of street maintenance has been the degradation of the streets themselves. Evaluating the condition of the City’s Streets is accomplished using the Pavement Condition Index (PCI). In 2012, the City’s Pavement Condition Report found the City’s weighted average PCI for the entire City network of streets was 76. In May of 2013, the City’s consultant, prepared the initial Safe and Sustainable Streets Infrastructure Study. This study looked at future funding needs for capital street maintenance and the ongoing base level street maintenance services.



In 2014, the weighted average PCI for the network had fallen to 70 and the Pavement Management Report identified a backlog of \$20.5 million. At the current level of funding, the City’s weighted PCI would fall to 65 by 2018. Since it costs less to maintain roads in good condition than bad, investing early to keep the weighted PCI higher is critical. As demonstrated in the adjacent chart, the maintenance cost grows much faster as the PCI drops.

Funding

The City funds ongoing base service street maintenance activities through the General Fund and Gas Tax Revenue, while the capital pavement rehabilitation program is funded primarily through the streets fund which receives revenues from gas taxes (via VTA), vehicle registration fees and the One Bay Area Grant. Over the last two years, the City has supplemented capital funds with dollars from the General Fund, but this is not projected going forward and not included in the existing General Fund five year forecast.

Base Service Level Funding

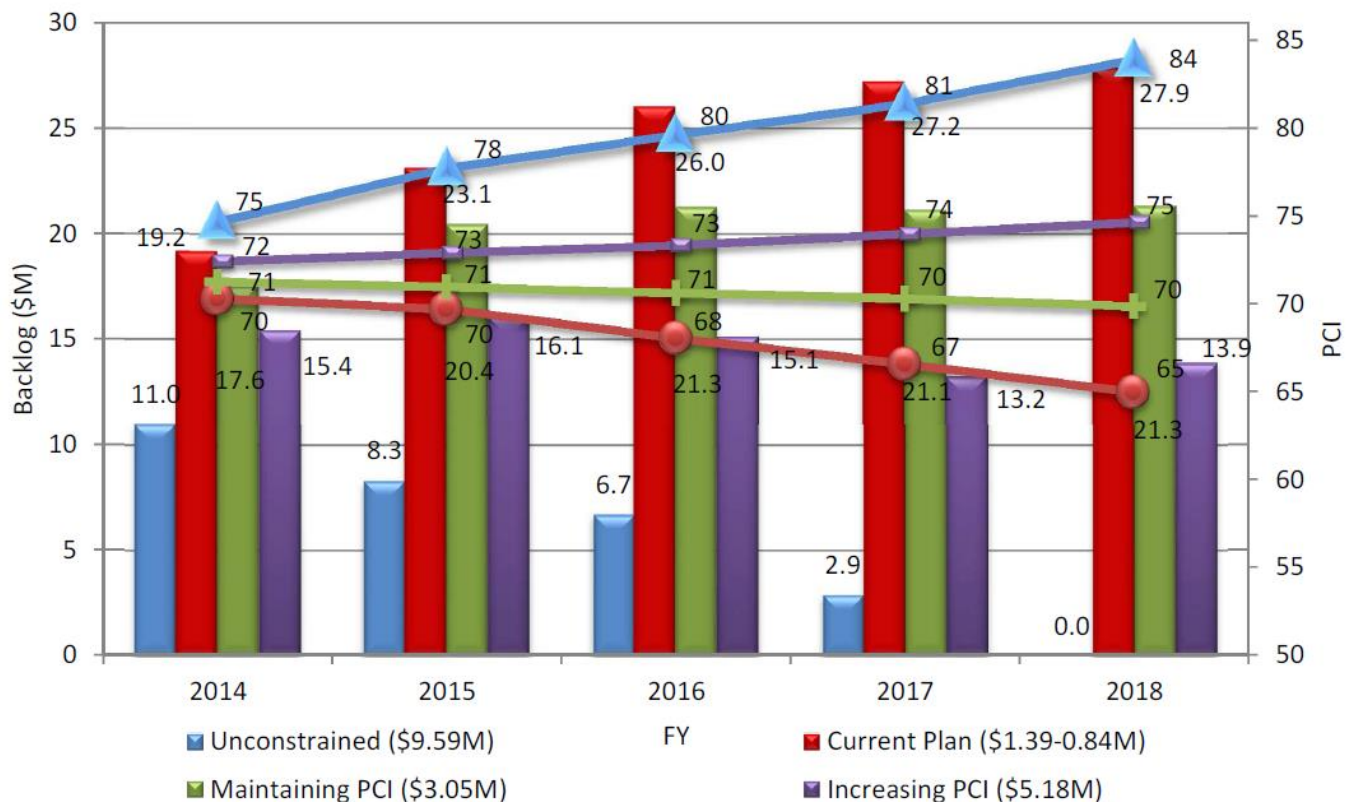
The Community Services Maintenance Team is responsible for the day-to-day maintenance of streets for the City. A combination of City employees and contract services are used to perform regular street maintenance. The 2013 Sustainable Streets Study identified that additional funding was needed for base street maintenance services, including ongoing funding of \$368,000 annually and one-time funding of \$107,000. Over the last one and a half years, the City Council has increased investment so that many of the unfunded maintenance needs have or will be met through General Fund investment or investment from other funds in specific project areas. The current additional funding need has been reduced to \$155,000 annually and \$43,000 in one-time funding. An outline of the current needs is available in Table 4.

TABLE 4. CURRENT VERSUS SUSTAINABLE STREETS - OCTOBER 2014 (1,000s)						
BUDGET ALLOCATION SCENARIO 3	FY14/15	FY15/16	FY16/17	FY17/18	FY18/19	TOTAL
Pavement Mgmt Program (PMP)						
Current PMP CIP Budget Allocation	2,297	753	753	753	753	5,309
Sustainable Funding	5,200	5,200	5,200	5,200	5,200	26,000
Funding Gap	2,903	4,447	4,447	4,447	4,447	20,691
Base Maintenance Services Division						
Current Budget Allocation	1,888	1,954	2,024	2,097	2,097	10,060
Unfunded Base Maintenance Services						
<i>Downtown Park Lot Slurry & striping</i>	<i>Now funded through CIP for Parking Lots.</i>					0
<i>Concrete/brick Paver Repairs</i>	12					12
<i>Sidewalk Repairs</i>	<i>Now funded through CIP - Safe Routes plus 1 time General Fund</i>					0
<i>Curb & Gutter Repairs</i>	<i>Infusion. Annual Maintenance Budget increased to \$50,000 annually.</i>					0
<i>Repaint Colored Curbs</i>	32	32	32	32	32	160
<i>Replace Aging Wood Streetlight Poles</i>	5	5	5	5	5	25
<i>Renovate Medians</i>	25	25	25	25	25	125
<i>Repair & Renovate Brick Planters</i>	<i>Will be completed in downtown renovations.</i>					0
<i>Prepare & Maintain Street tree Inventory</i>	10	2	2	2	2	18
<i>Remove/Replace Street Trees</i>	38	38	38	38	38	190
<i>Regular Street Tree Trimming 4 Year Cycle</i>	<i>Now funded in Annual Maintenance Budget.</i>					0
<i>Storm Drain Pipe & Culvert Inspection & Repair</i>	5	25	5	5	5	45
<i>Storm Drain Pump Station Rehab Amortization</i>	50	50	50	50	50	250
Sustainable Base Maintenance Services	2,065	2,131	2,181	2,254	2,254	10,885
Funding Gap for Base Maintenance Services	177	177	157	157	157	825
Total Funding Gap for Sustainable Streets	3,080	4,624	4,604	4,604	4,604	21,516

Note: This PMP CIP Fund 308 Budget Scenario would yield an estimated **PCI of 75**

Capital Improvement Funding

Capital improvements for street maintenance are managed by the Engineering Division of the Public Works Department through the City's annual Capital Improvement Program. Over the last two years, the City has invested one-time grant dollars augmented by one time General Fund dollars to increase the amount of funds used on pavement rehab projects. With the current backlog of street maintenance (\$20.5) million and the current PCI (70), the next chart provides information on how various levels of funding would impact the City's PCI rating and the maintenance backlog.



Investing at a level that increases PCI from its current condition is important, because investing enough to just maintain the current PCI will not reduce the backlog of maintenance and will end up costing the City more in the long run. By investing at a level that increases the PCI, the backlog of street maintenance will stabilize by 2018 and continue to gradually fall in the long term. Investing at a level that only maintains the current PCI will not reduce the backlog of maintenance and will cost the City more long term in both capital costs and ongoing base level maintenance costs.

Policy Discussion

To eliminate the backlog of street maintenance over the next five year period and increase the PCI to 84, an additional investment of \$9.8 million annually would be needed. It is estimated that an additional \$4.4 million would be needed annually to return the City's network of streets to an average weighted PCI of 75 and reduce the backlog to approximately \$14 million. The third scenario would require an additional annual investment of \$2.4 million annually and would result in a slight increase in the maintenance backlog.

At the current level of funding for street maintenance, the City will experience declines in the condition of the City's streets, which will in turn begin to impact and increase the level of base services and the deferred maintenance for streets will grow to a staggering \$27.9 million by 2018 - which would represent a 50% increase over five years. At this rate, the City's streets infrastructure will be in jeopardy. This degradation and funding backlog will only continue to mount unless a new sustainable revenue source can be identified, current General Fund services are significantly reduced and funding is reallocated to streets, or new revenue can be generated through industrial and commercial development. To reduce services in other areas to fund the \$4.4 million needed to maintain the City's streets sustainably, a 20% reduction in other vital services funded through General Fund discretionary revenue (Police, Fire, Parks, Admin Services, etc) would be required.

There are many questions that require discussion to address street maintenance funding. These include, but are not limited to:

1. Should General Fund discretionary revenues be prioritized to support street maintenance, which would require reduction in other services?
2. Should the City explore the development of a new tax revenue source?

Parks and Trails

The City of Morgan Hill has parks, trails and open space totaling over 300 acres of which 60 are maintained. Parks in Morgan Hill are funded in one of three ways, that include:

1. City Parks and Trails – Owned by the City and funded through the Park Maintenance Fund and General Fund.
2. Home Owners Association (HOA) Parks – Privately owned and funded by residents of the HOA.
3. Landscape Assessment District Parks – Owned by the City and funded by a limited number of residents within the assessment district for a specific park.

This section refers specifically to the maintenance of the first category, which includes parks, bicycle and walking trails, and the Civic Center outdoor spaces. These areas include a wide variety of amenities including: playgrounds, basketball courts, fields, tennis courts, picnic areas, lighting and many more. This strategy relies on growth to sustain the fund. Thus, as the City builds out, future funding could be an issue.

Revenue Support

Currently, base level park maintenance service is funded via the Park Maintenance Fund and supplemented by \$200,000 annually from the General Fund. The Park Maintenance Fund is funded through voluntary contributions from developers in the City's Residential Growth Control System process.

Base Services

Park Maintenance activities are managed by the Community Services Maintenance Team. Maintenance functions are performed by both in-house staff and via contract. It is estimated that base level City park and trail maintenance services are funded at an adequate level to be safely used and to protect the City's assets in these areas. However, the level of service for

these areas is not “top notch” and City parks would be considered at a level 3 or “Adequate” when applying the City’s previously developed Park Maintenance Numeric Rating System. Increased funding of base level services could improve aesthetics and user experience, but would not considerably increase sustainability of park and trail infrastructure.

Capital Repair and Replacement Funding

Table 5.

City Parks and Trails	Annual Unfunded Replacement
Community	224,557
Galvan	109,352
Paradise	38,106
Diana	31,052
Nordstrom	47,407
Jackson	17,201
Howard Weichert	7,235
Sanchez	3,188
Skate Park	23,219
Civic Center	47,026
Trails	37,429
Total	585,771

The recently developed Park Asset Replacement Plan identifies over \$6 million in future replacement needs stretching over the next 50 years, with a total unfunded annual replacement cost of \$586,000. No funds have been set aside for this replacement, although a past practice has been to use the Park Maintenance Fund for annually identified replacement projects. However, with the Park Maintenance Fund now funding the base level maintenance, drawing down the fund for capital replacement and repair projects would have an impact on sustainability of funding for base level operations.

Policy Discussion

When unfunded replacement needs to occur in parks, it is currently viewed on an annual project-specific basis and weighted against other projects of a citywide nature. In some cases, the life cycle of equipment is extended through repairing versus replacing equipment. In other cases, a choice may be to remove an asset. For example, turf could degrade to a point where it is in poor condition, but this would really only result in a decrease in user experience. Conversely, while a playground could degrade to a point where it must be removed for safety standards and, if not funded, would not be replaced. This funding shortfall for future replacement and repair of City Parks is a new discussion. Some policy questions that should be explored in this area include, but are not limited to:

1. Should a replacement/repair fund be established and funded for future park maintenance needs?
2. Should a new tax revenue source for parks be explored?
3. Should future park development be slowed until sustainable funding for existing parks can be established?

Landscape Assessment Districts

Revenue Support

Landscape Assessment District (LAD) funds are derived from special property assessments to support City maintenance services in park and landscape areas within residential developments that are located in the District boundaries. Proper maintenance of the properties benefits the owners. Assessment charges are collected by the County on property tax rolls and remitted to the City. There are currently 20 subareas in the LAD that include a total of 757

properties. Of these 20 subareas, 7 contain parks. Each lot within a specific subarea is assessed the same amount to obtain the level of service desired by the subarea residents.

Base Services

Base level maintenance services are provided based on the subarea's available funding. Many of these areas are funded and maintained well, while others are limited to weed abatement only.

Replacement Funding

To some extent, replacement funding for each subarea is addressed by creating a fund balance. Each subarea has an established fund balance reserve target based on the size, maintenance requirements, and amenities of the subarea. However, in the case of the LAD subareas which contain parks, the fund balances maintained would not be sufficient enough to replace or repair major park components. An outline of the LAD park subareas and their unfunded annual replacement can be viewed in Table 6.

Table 6.	
LAD Subarea Parks	Annual Unfunded Replacement
Oak Creek	39,925
Hamilton Square	5,351
Mill Creek	4,675
Rose Haven	9,894
Stone Creek	9,385
Diana Estates	15,048
Belle Estates	3,848
Total	88,126

Policy Discussion

LAD subareas with parks provide a unique challenge. The parks are open and available to use for the entire community, but are paid for by a specific set of residents located in the LAD subarea. In essence, a small percent pay for amenities used by many. A park like Oak Creek Park, which is large, well used and has insufficient replacement dollars could run into a scenario where the park playground needs to be replaced, but there are not available funds to do so. This scenario will eventually play out should policy and funding changes not be made. Most LAD subareas are at the max assessment cap, which means an increase for funding would need to be approved by voters in that subarea. In the past, LAD residents have shown reluctance to increase their own taxes for increased maintenance, resulting in some subareas receiving the bare minimum maintenance services. Policy questions for LAD Parks include:

1. Should assessment be raised in those subareas where capacity exists to plan for future replacement of park amenities?
2. Should a City-wide LAD or Community Facilities District for all City owned Parks be explored?
3. Should supplemental funding be used to ensure that LAD Park resources are maintained when assessment funds do not cover the cost of maintenance?

Building and Facility Maintenance

The City owns 12 facilities that are operated for a variety of public purposes including facilities operated and maintained by the City and others operated and maintained by partner organizations. These facilities include the two City Fire Stations, City Hall/Development Services Center, Council Chambers Building, Police Station, Corp Yard, Library, Aquatics

Center, Centennial Recreation Center, Community and Cultural Center, Friendly Inn Non-Profit Center, El Toro Youth Center, and Outdoor Sports Center.

Revenue Support

Maintenance of City facilities is funded via the fund that uses the facility. The City Recreation Centers, although part of the General Fund, recover costs through user fees for operations including facility maintenance. Other City facility maintenance funding is provided through the funds that fund the departments that use each of the facilities. For example, the maintenance of the Corporation Yard is funded through the Water Fund, Sewer Fund, Park Maintenance Fund and General Fund.

Base Services

Facility maintenance is managed by the Community Services Department and Community Development Department. In some cases, facilities are maintained through agreements with partner organizations (CALFIRE, County Library, and the Morgan Hill Youth Sports Alliance). It is believed that current base level maintenance services are fully funded and being provided at an adequate level throughout the City facilities.

Replacement Funding

In most cases, as each facility was constructed and opened for use, the City developed a replacement schedule that addressed the major components of each facility. This schedule has been funded by annual operating budget allocations. Replacement schedules were not developed for the Outdoor Sports Center and Friendly Inn while other replacement schedules for some City buildings were not comprehensive as others. Staff updated or created current schedules as a component of this report. Upon conclusion of this update, it is estimated that the facility replacement fund is underfunded by \$514,000 annually. Table 7 outlines each facility, current replacement funding and recommended funding.

Table 7. Facility Replacement	Current Annual	Recommended Annual	Funding Gap
Aquatics Center	\$ 55,441	\$ 203,405	\$ 147,964
Centennial Recreation Center	\$ 90,499	\$ 230,322	\$ 139,823
Community and Cultural Center	\$ 65,000	\$ 72,279	\$ 7,279
Council Chambers Building	\$ 10,710	\$ 37,022	\$ 26,312
Corporation Yard	\$ 5,290	\$ 21,747	\$ 16,457
Development Services Center	\$ 27,677	\$ 26,387	\$ (1,290)
Friendly Inn	\$ -	\$ 12,517	\$ 12,517
El Toro Youth Center	\$ -	\$ 6,620	\$ 6,620
Police Department	\$ 74,431	\$ 94,731	\$ 20,300
Outdoor Sports Center	\$ -	\$ 172,793	\$ 172,793
Fire Stations	\$ 60,000	\$ 25,404	\$ (34,596)
Library	\$ -	\$ -	
Total	\$ 389,048	\$ 903,226	\$ 514,178

There were some key factors that created a significant change in the recommended annual funding of facility replacement for a few facilities. These factors are outlined below for the facilities that are impacted.

Aquatics Center (AC) – The AC was constructed by the Redevelopment Agency in 2004 and ownership was transferred to the City of Morgan Hill. The Community Services Department budget includes an annual contribution to the Building Replacement Fund for the annual depreciation of the major building and facility systems. This plan however is underfunded as the replacement schedule originally did not include some very significant pool related components. Two of the largest factors are replacement of the pool deck and pool heating components.

Centennial Recreation Center (CRC) – The CRC was constructed by the Redevelopment Agency and opened in the City's centennial year, 2006. Ownership was transferred to the City which, through the annual Community Services budget contributes to the Building Replacement Fund. The expansion of the CRC in 2010 was paid for by the RDA since the facility is located in the former Project Area and specifically included in the Redevelopment Plan. Similar to the Aquatics Center, after updating the replacement schedule it is believed the CRC's future replacement is underfunded. The largest factors in this area include adding the solar panels at the CRC to the future replacement funding.

Community and Cultural Center (CCC) – The CCC was constructed by the Redevelopment Agency in 2001 and ownership was transferred to the City of Morgan Hill. The Community Services Department budget includes an annual contribution to the Building Replacement Fund in an amount equivalent to the annual depreciation of the major building and facility systems. The funding is adequate as only a small adjustment would be needed.

El Toro Youth Center – The El Toro Youth Center is leased to the Boys and Girls Club of Silicon Valley. The City provides the Boys and Girls club with annual funding to subsidize operations and funds maintenance of the building through the General Fund. Currently, there is no contribution to the replacement fund for the facility. It is recommended that contributions begin to be made.

Friendly Inn – The Friendly Inn has served the community in a variety of roles for over half of a century. It was renovated by the Redevelopment Agency in 2010 as a non-profit center. It currently houses 11 non-profit organizations, which each make use payments equal to their share of the ongoing maintenance costs based on the amount of space leased. In turn, base level maintenance services are paid for by the tenants, but there is not contribution to the Replacement Fund from the facility.

Outdoor Sports Center (OSC) – The Redevelopment Agency purchased the land for the complex and initially leased it to the California Youth Soccer Association to operate as a regional tournament facility. In 2007 the RDA improved the area with artificial turf fields, parking, lighting, and restrooms. The RDA conveyed the property to the City which, in turn, has leased it to the Morgan Hill Youth Sports Alliance (MHYSA) for a community serving sports center as well as host for regional tournaments. MHYSA makes annual improvements to the facility as part of its operating budget. As previously noted, a replacement schedule and annual operating funding were not initiated when the OSC came online. At the time of opening, the fees for the facility were directly related to recovering costs for operations. Including replacement funding would have more than quadrupled the user fee for use of the facility. Shortly after the initial opening, the City entered into a concessionaire agreement to operate the OSC and it was envisioned that a capital fund would be created. This has yet to materialize and neither the City nor the operator has contributed to such a fund.

City Council Chamber Building – The Council Chamber Building recently went through a \$2 million dollar renovation to become a state-of-the-art Chamber with new meeting room space, upgraded restrooms, and a new lobby area. It is utilized for City Council, commission, or other public meetings. The building has also recently begun housing a limited number of City staff that were no longer able to fit in the City Hall/Development Services Center Building. With the newly installed equipment, including state-of-the-art audio visual systems, funding the replacement of this equipment would be prudent.

City Hall/Development Services Center (CH/DSC) - The current CH/DSC is home to the City's Administrative Services Department, Community Development Department, Public Works Engineering Division, City Manager's Office, and City Attorney's Office. The building was remodeled in 2009 using the proceeds of a financing instrument called Certificates of Participation. The City agreed to make annual lease payments equivalent to debt service. The occupants of the building pay their proportionate share of the annual debt service. This type of financing is known as a "budgetary pledge" because no specific revenue source was dedicated to the debt service. The occupants also contribute annually to the Building Replacement Fund.

The Morgan Hill Library - The Library was constructed by the City of Morgan Hill and is leased to the County Library JPA for operations and maintenance. The capital costs were financed by a capital contribution by the RDA and a bond issue for a portion of the costs attributable to "new growth". The library was "sized" to accommodate the planned population of the City in 2020. The annual debt service is paid from available Development Impact fees and the General Fund. The City receives income from the library lease to the JPA which helps offset debt service.

Police Headquarters – In 2004, the City acquired an industrial building and upgraded the building to serve as an "essential public safety" building and Police headquarters. The costs were financed by issuing Certificates of Participation. Because the facility was sized to accommodate future growth, a portion of the annual debt service is paid by Development Impact fee revenue. The balance of debt service is paid as an annual operating cost of the Police Department and charged to the General Fund. The General Fund receives a small amount of revenue from a lease of current excess space to a private party. The annual budget also includes contributions to the Building Replacement Fund. The City's General Fund purchased an adjacent half acre of land for potential use as a storage yard for towed vehicles, or other future uses by the Police Department.

Corporation Yard – The city's field crews and equipment are housed at the "Corporation Yard" at Edes Court. The land including the adjacent Community Park was acquired by the City decades ago and initially developed as the city's first wastewater treatment facility. In the 1970's, the Corporation Yard was developed with the proceeds of bonds issued by a Joint Powers Agency which included improvements for the school "bus yard" north of Edes Court. The operating funds of the utilities (sewer and water) and the annual budgets of the streets and parks operations make annual contribution to the Building Replacement Fund.

Fire Stations – As part of the transition of CALFIRE in 2013, the City financed the purchase of its two fire stations. These loan payments are included in the Fire Department's annual operating budget and paid for by the General Fund. The base level maintenance of these fire stations is coordinated by CALFIRE as part of the agreement with the City and funded through the General Fund within the Fire Department's operating budget. The City established a

Building Maintenance Fund contribution of \$60,000 annually for replacement of Building Components. After the recent inventories conducted by staff, it is believed that this replacement funding can be reduced to \$25,000 annually.

Policy Discussion

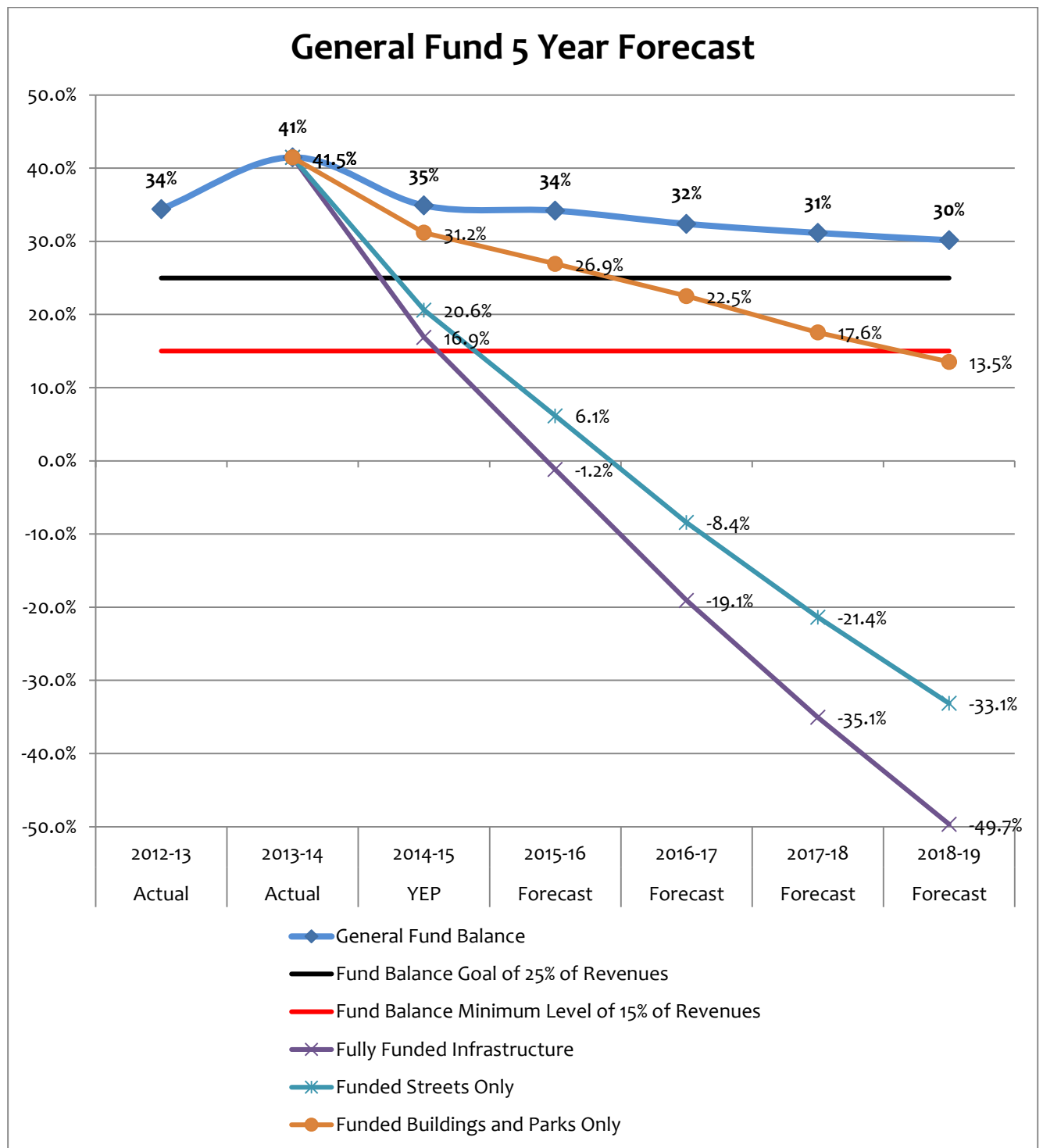
Three of the City's recreation center's make up the largest portion of the funding gap. The Aquatics Center and Centennial Recreation Center have continually improved their financial performance and replacement funding will be important to their continued success. Including the additional replacement fund costs in the annual operating budget for Recreation and Community Services would be consistent with the City's effort of "Balancing Cost Recovery and Community Access" at the City recreation facilities. The Outdoor Sports Center's concessionaire has provided the City with revenue each year. Additionally, the OSC has been a driver of economic development bringing hundreds of thousands of visitors to Morgan Hill annually. With the City reviewing the long term future of the OSC in the Spring of 2015, the need to plan for the future of the facility is critical. The synthetic turf fields at the OSC will be nearing the end of their expected life in the near future, and planning for their replacement is an important aspect of keeping the facility operating successfully. Overall policy questions for Building and Facility Maintenance include, but not limited to:

1. Should replacement funding at facilities be expanded to fully plan for all future capital replacement and repair costs?
2. Should fees be reviewed to assist in covering additional future replacement costs at our Recreation Facilities or should the General Fund invest more annually?
3. Who should be responsible for Outdoor Sports Center Future Replacement funding? The City? The operator? Both?

Possible Options for Infrastructure Maintenance Funding

The report clearly identifies that Street Maintenance has by far the largest need for additional infrastructure funding. However, the other infrastructure needs are also important and in some cases may create scenarios where multiple categories can be addressed simultaneously. Some possible options for addressing the City's funding gap include:

1. Dedication of General Fund Revenues - It is at the City Council's discretion to decide on utilization of any amount of General Fund dollars to support the maintenance of infrastructure. However, any use of General Fund resources would mean a reduction in service in another area and could have an adverse impact on the community. In alignment with the Council's Sustainable Budget Strategy, the current General Fund five year forecast provides for a General Fund reserve level of 30%. The graph below shows the impact on the General Fund forecast with various funding scenarios for infrastructure maintenance and no reduction to other service levels.



As the chart demonstrates, it is not possible to comprehensively address the funding gap and remain in compliance with the policy set in the Sustainable Budget Strategy. For all the scenarios outlined in the chart the downward trend demonstrates that other General Fund services would need to be reduced to fund infrastructure maintenance from the General Fund or new revenue sources would need to be realized.

2. New Tax Revenue Source – Some communities have successfully passed ballot measures to increase local taxes. This could be in the form of a bond issuance, sales tax increase, or a combination of the above. Pursuing a ballot measure is a complicated and expensive process that would require significant public discussion and involvement before moving forward.

3. New or Expanded Financing Districts - A financing district could be created which would be responsible for the care and maintenance of a portion of the City's Street Infrastructure or the City's Parks. Financing districts typically require approval (typically 2/3 majority) by the property owners within the district's boundaries. Revenues are generated from property owner approved assessments, property tax increments, or voluntary diversion of property tax revenues. It may be possible to expand the City's current LAD to be all encompassing of the City. There are a variety of opportunities for financing Districts in addition to the current LAD. The processes for creation of these districts is complicated and detailed review would be needed to determine the most appropriate for the City's needs.

4. Attempt to Increase LAD Assessments – This would be a small step towards only dealing with the unfunded maintenance in the LAD. Even if successful, this will not have a significant impact on the overall infrastructure maintenance funding need. Staff will be able to review this as part of the annual LAD assessment process.

5. Increase User Fees – This option would only be available for the Recreation facilities that charge a fee for service. This does fit in the current Recreation and Community Services model and would require raising rates for users to ensure cost-recovery included fully funding future replacement. The soon to be started Community Development fee study, will also need to include all costs.

6. Increase General Fund Revenues through Economic Development – Morgan Hill continues to thrive in attracting businesses and the improvements to the downtown will support this going forward. However, the infrastructure funding gap may be too large for this to be successful in the near term. For example, if City were hoping to offset the infrastructure funding gap through increased sales tax revenue, it would need to grow by over 65% from current levels.

Recommended Next Steps

The alternative funding options listed above are intended to be the start of the discussion to address the funding gap for City infrastructure maintenance. To move forward in addressing the identified needs it is recommended that the Council start with the following next steps:

1. Discuss infrastructure funding gaps by category and prioritize the needs.
2. Discuss the policy questions posed in this report as well as others relevant to the issue.
3. Identify and discuss funding alternatives for the City to fund infrastructure maintenance.
4. Actively participate in state and regional infrastructure funding advocacy and planning.

Appendices

- A. Pavement Management Program Report
- B. 2014 State of California Local Streets and Roads Assessment